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## CANADIAN CULTURAL INDUSTRIES EXEMPTION FROM NAFTA-ITS PARAMETERS

*Ronald G. Atkey\**

### I. INTRODUCTION

Technically, this could be quite a short Article. The Canadian government has never formally invoked the cultural industries exemption under either NAFTA (since January 1, 1994) or the Canada-United States FTA (1989-93). Accordingly, it has not been necessary for any third party adjudicator to look at the scope of the definition of "cultural industries."<sup>1</sup> Neither has it been necessary for any third party adjudicator to examine the nature and extent of permitted retaliation, i.e., "measures of equivalent commercial effect," in response to actions that would have been inconsistent with FTA or NAFTA, but for the cultural industries exemption.

The most that one can say about this permitted retaliation, on the plain meaning of the words<sup>2</sup> is that there must be commercial parity in terms of the dollar value of the trade or investment affected or likely to be affected by the inconsistency. It is my understanding that there may be written interpretations to this effect operative in both the Office of the United States Trade Representative (USTR) and the Canadian Department of Foreign Affairs and International Trade (DFAIT), but that is the extent of it. There also appears to be some agreement on both sides of the border that any retaliatory measures taken need not be limited to the same trade sector or industry which was subject to the inconsistent treatment under the free trade rules although this point has also never been formally considered by any third party adjudicator.

In summary, if this Article were to end here, the cultural industries

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<sup>1</sup> U.S.-Canada Free Trade Agreement, Jan 2., 1988, 27 I.L.M. at art. 2012 (hereinafter FTA). North American Free Trade Agreement, Sept. 6, 1992, Ch. 17, 32 I.L.M. 296 at art. 2107 (hereinafter NAFTA).

<sup>2</sup> FTA *supra* note 1, at art. 2005(ii). NAFTA *supra* note 1, at 2106, Annex 2106).

exemption would warrant little more than a technical footnote, or at best be characterized as a "standstill arrangement" or political trophy extracted by the Mulroney government in the eleventh hour of the 1988 FTA negotiations to placate cultural nationalists in central Canada immediately prior to the upcoming election, with reluctant acquiescence from the U.S. negotiators.

The fact is, however, notwithstanding the lack of formal invocation of the exemption, cultural industries currently occupy a significant portion of the dispute agenda between Canada and the United States for both trade and investment. Moreover, this dispute agenda involving cultural industries is growing year after year as both countries become emboldened by recent successes: Canada with the more restrictive broadcasting policy developed and applied by the Canadian Radio-Television and Telecommunications Commission (CRTC) most recently to direct-to-home pay-per-view services, and the United States with its successful challenge before a WTO panel to Canadian discriminatory measures applicable to split-run magazines.

The extent to which cultural industries are tending to dominate the formal dispute agenda between Canada and the United States can be fully appreciated by a review of portions of a key document published by the USTR on March 31, 1997 entitled, *1997 Foreign Trade Barriers*. In the section reviewing Canada, the Report discusses some twenty barriers to trade and investment between Canada and the United States. Many of these Canadian barriers affect cultural industries: magazines, sale of audio tapes, delisting of non-Canadian broadcasting services, non-proprietary rights condition applicable to direct-to-home (DTH) pay-per-view, revenue splitting condition applied to DTH pay-per-view, DTH audio services, basic telecommunications services, border broadcasting, foreign investment in publishing, and foreign investment in film distribution. In effect, it is fully one-half of the Canada-U.S. agenda of foreign trade barriers.

So the reality is, cultural industries exemption notwithstanding, there are significant trade and investment issues where Canada and the United States are at odds and which will, in all likelihood, have to be resolved outside the dispute settlement mechanisms under NAFTA. Indeed, the cultural industries provisions of the FTA and NAFTA, when read together, make it clear that the consultation and dispute settlement or arbitration provisions under NAFTA, normally available when there has been a nullification or impairment of any benefit under NAFTA, are specifically not available when the dispute involves cultural industries

(Article 2011(ii) of FTA, Annex 2106 under NAFTA).<sup>3</sup>

In short, the more appropriate title of today's panel might have been "Canada-U.S. Cultural Industries Disputes Outside of NAFTA."

## II. THE CANADIAN PERSPECTIVE

Before examining the Canadian instruments for protecting culture, it is a useful if not frustrating exercise to try to define Canadian culture. To put it directly: how are Canadians different from Americans?

In my own simplistic way, I have often thought of Canadians as gentler, more polite, less aggressive, insecure but more tolerant, accommodating bilingualism, embracing multiculturalism, finding strength in diversity, resourceful, traditional, and committed to peace, order, and good government. Does this have anything to do with culture? I think it does. It is part of what flows from our Canadian way of doing things and represents many of the shared values of Canadian individuals and institutions.

One of our most famous authors, the late Robertson Davies, described our cultural differences in terms of psychology. In a U.S. magazine article written at the time of the introduction of the FTA in 1989, he quoted a Canadian artist, saying, "The U.S. frontier is in the West and the hero is an outlaw; the Canadian frontier is in the North and its hero is a policeman." Robertson Davies then told his American readers, "Your aspiration toward life, liberty and the pursuit of happiness is one that we admire, but our own is for public order and good government."

That is the conventional view in Canada. But it took a somewhat irreverent book on Canadian pop culture called *Mondo Canuck* published last fall and written by two young television journalists, Geoff Pevere and Greig Dymond, to strip away all the veneer and get at the root of what being Canadian is all about. Let me quote at length from their

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<sup>3</sup> My fellow panelist John Ragosta will outline for you how the U.S. and Canadian technical interpretations of the NAFTA exemption provision differ. The Americans apparently read the NAFTA provision as simply repeating the FTA provision: a party is permitted to take actions inconsistent with NAFTA involving cultural industries, but the other party has an automatic right of retaliation if its industries are harmed by this protection. Some Canadian officials argue that NAFTA has literally, rather than functionally, transplanted the FTA system for cultural industries. This is to suggest that only the FTA, and not NAFTA, obligations are subject to the derogation-and-right-of-retaliation scheme, leading to the possible result that, say, intellectual property obligations and certain service areas (not covered by FTA) could be breached by Canada without NAFTA-based U.S. retaliation. So far, this difference of opinion in interpretation has been proceeding more on the academic rather than practical or political level although there are no assurances that this state of affairs will continue indefinitely. FTA, *supra* note 1, at art. 2011(ii). NAFTA, *supra* note 1, at Annex 2106.

## introduction:

To grow up in those parts of this country called "English Canada" is to grow up with a peculiar certainty of the in-betweenness of things. It is to come to define yourself more readily as what you aren't than what you are, and to learn to register constant equivocation merely by the simple rhetorical attachment of a tentative "eh" to the end of otherwise declarative statements, as in "Hey, give back my damned wallet, eh?" Because neither your measuring nor monetary systems correspond with the most influential cultural, political and economic presence on your continent, as a Canadian you learn to do metric and financial conversions almost as early as you learn to skate. Though your background may be Chinese, Romanian, Ojibway and Haitian, you know the proper French phrase for things like "high in dietary fibre," and "now enriched with six essential vitamins" from staring daily at bilingual cereal boxes. You grow up strafed by the relentless barrage of American media, yet every time you reach for change you realize you still share a queen with the tiny, distant island which was once your colonial master. To be a Canadian is to live in the space between certainties, to dwell in the gap that separates conviction from speculation. To be Canadian, in other words, is to exist in a state of constant becoming.

This explains why there may be no other country which has managed to turn the process of self-definition into such an industrious national pastime: next to hockey, watching TV, and making long-distance phone calls, Canadians seem to enjoy nothing more than sitting around and fretting about who they are. And even more so lately: what with the unsettling prospect of Quebec separation, the continued depletion of the public sector and the post-multicultural distrust of nationalism generally, the process of anxious self-examination has reached a feverish pitch. Indeed, so much of our indigenous cultural activity . . . seems preoccupied with the question of defining Canada, one wonders if we'd have any indigenous cultural activity without the question to ask. Imagine it: if Canada *were* actually defined to the satisfaction of everyone involved, what would Canadians do for rhetorical amusement? After all, it may only be uncertainty, but it's *our* uncertainty. The fact is, in the absence of any other unanimously endorsed cultural characteristic, it's all we've got. Without doubt, we're nothing.<sup>4</sup>

Assuming that this distinctiveness is worth protecting, and I dare say most Canadians think it is, how have we done so far? Do we have cultural industries in Canada that are able to preserve and nurture this distinctiveness in the face of the United States entertainment juggernaut spewing American culture across our borders from New York, Nashville, and Hollywood? The official line from Ottawa is that we have not done very well. Listen to the litany of grievances coming from the mouths of Trade Minister Art Eggleton and Canadian Heritage Minister Sheila

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<sup>4</sup> GEOFF PEVERE & GRIEG DYMOND, *MONDO CANUCK: A CANADIAN POP CULTURE ODYSSEY*, Prentice Hall Canada, 1996.

Copps. Every time they have had a chance to speak on this subject over the past year, they recite this mantra:

- Three-quarters of the television watched every night by Canadians is of foreign origin, usually American.
- Four out of every five magazines sold on the newsstands in Canada are foreign magazines, usually American.
- Ninety-six percent of the screen time at Canadian theatres is taken up by foreign films, mainly from the United States.
- Seventy percent of the content on Canadian radio stations is non-Canadian, usually from the United States.

This whiney attitude towards the Americans carries over to the national media in Canada. *Maclean's*, which purports to be Canada's weekly newsmagazine, and which has prospered thanks to protectionist tax measures and a huge postal subsidy, is sometimes the worst offender. Instead of celebrating the worldwide success of Canadian author Michael Ondaatje who wrote *The English Patient*, *Maclean's* cover story, which came out last month at the time of the Academy Awards, was headlined *The Canadian Patient: How Our Book Became Their Movie*.

But does this whining reflect the true situation, or tell the whole story? I have done a bit of a market reality check and found significant achievements in the same areas where the Ministers and the media have pumped out tales of woe:

- Canadian-produced television series are doing better than ever before, both domestically and internationally; consider the recent success enjoyed by *Traders*, *Due South*, *This Hour Has 22 Minutes*, *Newsroom*, *Kung Fu: The Legend Continues*, *The X-Files*, and a large number of animation films produced by Cinar of Montreal and Nelvana of Toronto.
- Over three-quarters of all magazines read regularly by Canadians are delivered into their homes through subscriptions and controlled circulation; ninety-four percent of these are Canadian-owned publications.
- Approximately twenty percent of the films exhibited at Canadian theatres are now produced by Canadian-owned companies. On a week-by-week basis, approximately thirty percent of the top grossing films in Canada are now distributed by Canadian-owned distributors. This significant improvement has resulted in part from the designation of Universal (formerly MCA) by Industry Canada as a Canadian-owned company following its acquisition by Seagrams, which is controlled by the Bronfman family of Montreal and New York.

• In worldwide record sales in 1996, Shania Twain sold ten million copies of *The Woman in Me* (without even going on tour, except for an overnight at the White House). Alanis Morissette has sold almost thirty

million copies of *Jagged Little Pill* (over two million alone in Canada), and Celine Dion has sold twenty-one million copies of *Falling Into You*. These three Canadian women have dominated prime-time music radio and television for the past two years in both Canada and the United States.

◦ Canada's exports of cultural goods and services now exceed three billion dollars, an increase of almost 100% since 1990. The United States represents over eighty percent of this market.

If there is any doubt that Canadian culture is flourishing, look at what the irreverent cynics, Geoff Pevere and Greig Dymond, have to say in *Mondo Canuck*:

Certainly, there is more Canadian popular culture than ever, but it's also more *popular* than it ever was. Indeed, when one begins to list the names of Canadians who have made an impact on global entertainment over just the past few years, the results are nothing short of staggering: Bryan Adams, James Cameron, Jim Carrey, Doug Coupland, Celine Dion, Atom Egoyan, David Foster, k.d. lang, Pamela Anderson Lee, Alanis Morissette, Mike Myers, Matthew Perry, Shania Twain, Steve Williams. And we repeat: that's just the past few years.

Here's our suggestion. What if, for a moment, we were to drop that conventional Canadian middlebrow disinclination toward popular culture-disinclination which is still very much alive and well-to suggest that Canada is every bit as distinct in its approach to schlock as it is to art, and that the former may indeed reveal vastly more of a national distinction than the latter. That it's possible to see as much of ourselves (if not more) in Mike Myers as it is in Margaret Atwood. That the Tragically Hip have as much to tell us (if not more) about the experience of living in post-Mulroney Canada as Peter Gzowski does. Moreover, what if, contrary to the established Canadian tradition of disowning anyone who dares to seek and find success elsewhere, we were to expand and ventilate our notion of what's Canadian to include what Canadians are doing on the global pop-culture stage? If one agrees first that there is something distinct about the way Canadians view and engage with the world, then why not allow for the possibility that our sensibility is a portable, flexible and resilient one, which influences what Canadians do no matter where we do it?

...

If one *does* begin to think about Canada in terms of the pop culture it produces, both nationally and internationally, one not only begins to move away from the us-versus-them national-victimhood model of the past, one in fact starts to see something so different as to be strikingly so: a "Canada" which is not only sly, dynamic, intelligent and resourceful, but one that's also a helluva lot more fun than the old one.<sup>5</sup>

Not to put too fine a point on it, but Canadian cultural industries

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<sup>5</sup> PEVERE & DYOMND, *supra* note 4.

are thriving. Many of our popular musicians have enjoyed international success and prosperity. Our television series are winning international awards and acceptance. Our better authors are awarded major prizes and receive critical acclaim throughout the English and French-speaking world. Even our film and television production and distribution companies have grown and prospered. Alliance, Astral, Atlantis, Cinar, Cineplex Odeon, Coscient, Malofilm, Nelvana, and Paragon are publicly traded companies with full access to Canadian capital markets for the purpose of expansion; Norstar and CFP have recently expanded their capital base through private placements. Canada has an ample supply of world-class actors, producers, directors, writers, and cameramen. The value of the Canadian dollar is an attractive incentive to international productions and union-management relationships are very positive. In Canada's largest province, Ontario, cultural industries are collectively the largest employer of individuals, second only to the auto industry.

Strangely, the most upbeat official comment on the development of Canadian culture comes from Statistics Canada, the government's statistical bureau. Here is the summary from the StatsCan quarterly bulletin dated Autumn, 1996 on International Trade in the Arts and Culture Sector:

The songs of Bryan Adams, Celine Dion, the Rankin Family, and k.d. lang; the novels of Margaret Atwood, Robertson Davies, Anne Hebert, and Antonine Maillet; the productions of Charles Dutoit, of le Cirque du Soleil, Robert Lepage, and Carbone 14; the films of Atom Egoyan, and Denys Arcand; and the renowned tenors Benn Heppner, Richard Marigison and Michael Schade, all have captured the attention of people around the world. And in so doing, they have helped forge an identifiable image for Canada, a sense of what we stand for, of what kind of society we are, and of course, the kinds of cultural products we produce.

Canada's exports of cultural goods and services are growing at unprecedented rates (increasing almost 83% between 1990 and 1995 to reach just under \$3 billion). These export results are not simply due to changes in the value of the Canadian dollar. Far more important has been the growing international demand for Canadian cultural goods and services, and acceptance by individual artists and companies, both large and small, of the challenge of the global marketplace.

Exports of cultural goods (excluding cultural equipment) increased by 125% overall, to reach \$1.2 billion in 1995. This rapid growth in our exports is diversified and is taking place in almost all major cultural export sectors such as publishing, film and sound recording. International trade data (on commodity exports) indicate that between 1990 and 1995 exports of books went up by 151% to \$246 million; films by 133% to \$65 million; and recordings by 324% to \$111 million.

The United States continues to be overwhelmingly our most important export



market for all cultural fields, accounting for 84% of exports of cultural goods in 1995 (ranging from 75% of our export sales for sound recordings to 99% of our newspapers and periodicals).<sup>6</sup>

Given typical Canadian deference to authority, can anyone seriously quarrel with StatsCan, that irrepressible institutional purveyor of hard cold facts?

### III. CANADIAN INSTRUMENTS FOR PROTECTING CULTURE

The Canadian approach has always been to attempt to craft its cultural legislation or regulatory action in a manner which is intended to be consistent with NAFTA and other international trade obligations rather than to rely on any cultural industries exemption to excuse actions that are otherwise discriminatory. These measures typically have taken the form of foreign investment and ownership restrictions, Canadian content rules, regulatory/licensing conditions, tax incentives, and subsidies. Up until the successful USTR challenge at the WTO on magazines, this approach had been successful.

#### A. *Investment Policy*

Film industry investment is a good example. Canadian policies established in 1988 prohibit foreign takeovers of Canadian-owned film distribution firms. They allow foreign investors to establish new distribution firms for proprietary products only. Indirect or direct takeovers of foreign film distribution firms operating in Canada are only allowed if the investor undertakes to reinvest a portion of its Canadian earnings (usually up to ten percent of gross revenues).

For almost ten years, these policies sustained the status quo, with the major Hollywood studios established in Canada prior to 1988 (Disney, Paramount, Warner Bros., MCA/Universal, Columbia Tristar, MGM/UA, and Twentieth Century Fox) being permitted to continue to build their film and television distribution businesses. In 1996, MCA/Universal became "Canadian" under the Investment Canada Act following its acquisition by Seagrams, but it has not changed materially its film and television production and distribution business which is run primarily from the United States. If it wanted, Universal could acquire or establish Canadian cultural businesses free of review by Investment

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<sup>6</sup> STATISTICS CANADA, INTERNATIONAL TRADE IN THE ARTS AND CULTURE SECTOR, Ottawa, Autumn, 1996.

Canada.

However, Canadian production and distribution firms have taken the lion's share of new growth in Canada over the last few years. There are now nine publicly traded Canadian-owned film and television production and distribution companies, whereas in 1988 there were none.

The restrictive nature of Canadian investment policies recently came into focus with a high-profile application to Investment Canada filed last year by Polygram, based in the United Kingdom and the Netherlands, to establish a new film distribution firm for non-proprietary products. Polygram argued both privately and publicly that it should be put on the same level playing field as the grandfathered (pre-1988) Hollywood studios. As an inducement to the Canadian government to change its policy, Polygram offered to reinvest a significant portion of its Canadian earnings in Canadian film production and development.

So far, Polygram has been rebuffed in its very public attempts to have this application approved. So it must content itself with a much reduced new distribution firm in Canada distributing only proprietary films (i.e., films for which Polygram owns the worldwide rights or for which it contributed more than fifty percent of costs up to the completion of the final negative).

Obviously, the USTR is quite content to let sleeping dogs lie since the Motion Picture Association of America (MPAA) member companies (i.e., the Hollywood studios), with their great influence in Washington, are all essentially grandfathered. However, there is some disquiet among U.S. interests at the Canadian government's disposition of the Polygram application since the outcome seems to have validated yet another precedent for discriminatory treatment in investment which could be invoked by Canada in other cultural sectors possibly against U.S. interests. Also, this decision represents a dangerous precedent in that it might be invoked by the Europeans against U.S. interests. From a Canadian perspective, the continued use of investment restrictions raises questions about the appropriateness of an inward-looking cultural policy. Given the fact that the Hollywood competition is effectively grandfathered, it is worth asking whether Canada would have benefitted more from the increased global opportunities its industry would have received from Polygram than it does by simply shutting Polygram out of Canada.

One can contrast the government's decision on Polygram with its decision in 1994 to allow Viacom, Inc. of New York to acquire indirectly all of the Canadian interests of Paramount Communications, Inc., also a U.S. company. Included in the Viacom undertakings negotiated in return for allowing the transaction to proceed in Canada was a commitment to provide international distribution of at least four Canadian fea-

ture films of suitable commercial quality before the end of 1999.

Foreign investment policy in Canada respecting the publishing of books is another example of the Canadian approach. In 1985, well before the FTA, the government of Canada established policies prohibiting non-Canadians from establishing new book publishing businesses or directly acquiring any existing businesses, whether Canadian or foreign-controlled. Up until 1992, this policy also extended to indirect acquisitions as a result of mergers and acquisitions of parent firms outside Canada, with divestiture of control to Canadians of the Canadian publishing business required within a period of two years at fair market price.

These restrictive policies were relaxed somewhat in January, 1992. First, direct acquisitions are permitted in extraordinary circumstances where a vendor is in clear financial distress and Canadians are first given a full and fair opportunity to purchase. Second, if a non-Canadian publishing business is to be acquired directly or indirectly by other non-Canadians then, instead of divestiture within two years, the foreign investor is required to negotiate specific commitments related to the development of Canadian authors, to support the infrastructure of the book distribution system in Canada (e.g., warehousing and order fulfillment in Canada, active participation in industry cooperative ordering/distribution/marketing endeavours), accessibility of the purchaser's Canadian marketing and distribution infrastructure or international network to interested compatible Canadian-controlled publishers on a contractual basis, and to education and research through financial and professional assistance to institutions offering programs in publishing studies.

These relaxed book publishing policies have been applied under the Investment Canada Act in several high-profile cases. In November, 1992, the Canadian government approved the acquisition of HarperCollins Canada Limited by News International plc, with the purchaser making significant undertakings of benefit to Canada under each of the four policy categories of the book publishing guidelines discussed above.

In 1994, the Canadian government approved the re-acquisition by Paramount Communications Inc. of a fifty-percent controlling interest in Ginn Publishing and Maxwell MacMillan Canada both of which had been the subject of a pre-1992 divestiture to the Canadian Investment Development Corporation (CIDC). Significant undertakings were given by Paramount Communications, Inc. and its publishing subsidiary, Prentice Hall Canada, related to development of Canadian authors, support of infrastructure, permitting accessibility for Canadian-controlled

publishers, and commitment to education and research. These undertakings, which were a matter of considerable political controversy because the controlling interest in these Canadian book businesses was passing from Canadian to foreign hands, were confirmed and adopted in late 1994 as part of the Investment Canada approval of the indirect acquisition of all Canadian cultural industries of Paramount Communications Inc. by Viacom Inc. of New York. In fact, the term of these undertakings was extended as a result of this subsequent acquisition for a period up to the end of 1999.

### *B. Import Policies*

Apart from investment policies, Canada has had a number of import policies applicable to cultural industries. The most notorious, of course, was recently struck down by the WTO panel on magazines. Tariff Code 9958, in place since 1965, essentially banned foreign split-run periodicals at the border in an effort to preserve Canadian print advertising dollars for the Canadian magazine industry. The WTO panel found that this measure was a clear violation of Article XI.1 of GATT 1994 which is a rule against quantitative import restrictions.

Another more subtle import restriction designed to promote Canadian magazines related to preferential postal rates. In general terms, there is a five to ten percent differential in postal rates between those magazines distributed by mail in Canada and those imported by mail. Moreover, there are a number of technical discounts available to magazines mailed domestically not available to those mailed from outside the country. The WTO panel struck down this differential in postal rates. Significantly, however, a more substantive measure that Canada has had in place for many years provides for funded or subsidized postal rates, available only to Canadian-owned magazines. The WTO panel found that this funded scheme was an acceptable subsidy under Article III.8(b) of GATT 1994 and was, therefore, not inconsistent with Canada's trade obligations. In practical terms, this means that a Canadian magazine can be mailed in Canada today for 8.6¢ while a foreign magazine would cost 38¢ to mail. This subsidy will continue until at least March 31, 1999.

### *C. Tax Policies*

The most important issue before the WTO panel on magazines involved Canada's attempt to use the Excise Tax Act to achieve a cultural objective favouring Canadian-owned magazines. To counter the introduction of a split-run edition of *Sports Illustrated* in 1993, the Canadian

government subsequently introduced an eighty-percent tax imposed on the value of advertising contained in all split-run magazines. Since the tax on its face appeared to be "country neutral," the Canadian government took the position that the tax was in full compliance with Canada's international trade obligations although clearly it was aimed at *Sports Illustrated Canada* and would not apply to Canadian-owned magazines since there were no Canadian split-runs that would be subject to the tax.

In response to the challenge launched by the United States under the GATT, Canada's main argument before the WTO panel, as well as the case under appeal, was that the tax was imposed on advertising services rather than the magazines themselves as goods. Therefore, it was the General Agreement on Trade and Services (GATS) that applied, not GATT 1994 which addresses trade in goods. GATS has no specific commitments regarding advertising services which is therefore tantamount to an exemption. In its most significant finding, the WTO panel rejected this approach and found that the spirit of global free trade and the express wording of various international agreements supported a more liberal view. Specifically, the panel found that GATT 1994 and GATS can coexist without either taking priority over the other. Moreover, the panel found that several precedents exist which permit a consideration of trade and services, including advertising services, under GATT. In its final ruling, the panel found that imported split-run periodicals were subject to an internal tax in excess of that applied to domestic split-run periodicals. While Canada argued that the tax applied only to the advertising contained as an input to the product, the panel noted that the tax was indeed applied to the magazine as a "good" since the tax was calculated on a "per issue" basis and did not apply to advertising services contained in other media, only to periodicals. Accordingly, the panel found that the tax constituted excess taxation applied to foreign split-run magazines in breach of Canada's commitments under GATT 1994.

In my view, the eighty-percent tax represented an overextension of Canadian policy which purported to pursue "national treatment" in principle, but not in practice. The demise of the tax before the WTO should not have been surprising, given the crisis-driven approach which gave rise to its creation. The Canadian government was pushed into this initiative by an overly aggressive Canadian magazine industry whose representatives actually conceived and drafted the measure, intending to take direct aim at *Sports Illustrated Canada*. Remember, this magazine was legally established, with the approval of Investment Canada in 1990 and Revenue Canada in 1993. Rejecting any compromise based on

grandfathering, the proponents effectively caused Canada to catapult its entire panoply of tariff and postal measures respecting magazines onto the world stage of the WTO, with the prospect of an uncertain legal result. Indeed, Canada refused to heed serious warnings within its own Parliament that the measure was a flawed piece of punitive tax legislation which was not necessary to maintain the government's policy against split-runs, and which might provoke an unnecessary trade war with the United States. The Canadian government also elected not to follow a recommendation of a Task Force created to consider the state of the Canadian magazine industry. Their recommendation would have provided limited "grandfathered" status for *Sports Illustrated Canada*. The result may be far more damaging to the longstanding protective legislative and regulatory regime for Canadian magazines and other cultural industries than would ever have been the case had reason prevailed when the Canadian magazine lobbyists first advocated a draconian solution without clearly and fairly identifying the problem. In fact, their solution in search of a problem may have now actually created one.

#### *D. Broadcasting Policy*

It is in the field of broadcasting that Canada is most aggressive in its protection of Canadian cultural industries—television broadcasting, cable television, direct-to-home satellite broadcasting, radio, and even aspects of telecommunications. Through a complex regulatory thicket which limits foreign ownership, imposes Canadian content quotas, requires domestic distribution commitments, and denies tax deductions for cost of advertising in foreign broadcast and print media when the advertising is directed primarily at Canadians, Canada has long-standing service barriers which were scarcely impacted by the FTA and NAFTA.

In fact, there are only four cultural areas which are not exempted from national treatment principles on a prospective basis by the FTA/NAFTA cultural industries exemption. The first relates to Article 1607(4) of the FTA, which provides that in the event that Canada requires the divestiture of a business in a cultural industry pursuant to its review of an indirect acquisition by an American, Canada shall offer to purchase the business enterprise from the American at fair open market value as determined by an independent, impartial assessment. This is the provision which caused the Canada Investment Development Corporation to purchase the controlling fifty-percent interest in Ginn Publishing and Maxwell MacMillan Canada in the late 1980s from Paramount/Prentice-Hall (later re-acquired by Paramount/Viacom in 1994).

The second exception relates to retransmission rights and the agree-

ment by both the United States and Canada to provide copyright protection to owners of programs broadcast by distant stations and retransmitted by cable companies.<sup>7</sup>

The third exception relates to the elimination of the requirement that a magazine or newspaper must be typeset and printed in Canada in order for advertisers to be able to deduct their expenses for advertising space in that magazine.<sup>8</sup>

A fourth exception related to the elimination of tariffs on any inputs to and products of the cultural industries such as musical instruments, cassettes, film, recording tape, records and cameras.<sup>9</sup>

Other than these cultural areas to which the FTA/NAFTA rules apply, Canada has not hesitated to develop and expand its broadcasting policy under The *Broadcasting Act* which lists among its objectives, "to safeguard, enrich and strengthen the cultural, political, social and economic fabric of Canada." The CRTC has been given a broad regulatory mandate by Parliament.

One of the CRTC's most significant policies developed under this mandate concerns a situation where a Canadian television programming service is licensed in a format competitive with that of a non-Canadian service authorized for distribution in Canada. In this instance, the CRTC can drop the non-Canadian service if the new Canadian applicant requests it to do so. This is exactly what occurred in June 1994 when the CRTC de-listed Country Music Television (CMT) and licensed a competitive new Canadian specialty channel, New Country Network (NCN). CMT, which has been doing business in Canada for about ten years prior to being delisted, subsequently filed a section 301 petition with the USTR seeking relief as well as seeking relief in the Federal Court of Canada. Eventually, trade action was averted when the new Canadian licensee reached a commercial resolution with CMT which involved the new licensee having access to the CMT name, programming and other licensing benefits in return for having provided CMT with a twenty-percent equity interest in the new licensee (the maximum direct foreign ownership permitted for a Canadian broadcaster).

Although the CMT de-listing is the most high-profile dispute to arise in recent times under this policy, there is no doubt that the policy has effectively deterred potential new U.S. entrants from attempting to directly enter the Canadian broadcasting market. Seeking status as an

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<sup>7</sup> FTA, *supra* note 1, at art. 2006.

<sup>8</sup> *Id.* at art. 2007.

<sup>9</sup> *Id.* at art. 401.

eligible satellite service under the sponsorship of a Canadian licensee is often touted as an easier route to Canada for U.S. television services given the onerous requirements of the alternative method of market access, becoming a licensed service by the CRTC. However, the threat of becoming delisted months or possibly years after establishing a business in Canada as a result of the CRTC's non-competition policy makes even this method of market entry an uncertain proposition.

In December 1995, the CRTC issued two national direct-to-home (DTH) satellite TV licenses and simultaneously, a number of DTH pay-per-view (PPV) licenses. The PPV licenses included two new conditions clearly aimed at U.S. programming, particularly feature films. First, it was made a condition of license that non-proprietary feature film rights must be acquired from Canadian-owned distributors. The effect of this condition will be to give Canadian film distribution companies significant market advantage if not a monopoly with respect to a majority of feature films which are increasingly "non-proprietary" in terms of their financial and corporate structure. A second condition of license was that revenues earned from the exhibition of all non-Canadian feature films must be split, on a title-by-title basis, one-third to the DTH service, one-third to the programming undertaking, and one-third to the producer/distributor. This mandatory fee cap further reduces the amount of revenue that a U.S. feature film producer can receive from exploitation of the film in Canada, and hence acts as a diminution of its intellectual property right and a restraint on its competitive position.

The U.S.-based film studios appealed these licensing conditions both to the Federal Court of Appeal and to the Canadian Federal Cabinet in 1996, but both appeals were unsuccessful. Of particular note is the Federal Court's determination that film distribution is a necessary aspect of the CRTC's broadcasting mandate appropriately subject to its jurisdiction. In my view, this judicial ruling constitutes a significant expansion to the CRTC's jurisdiction and will no doubt embolden it in its policy-making role in the future. As a result of these unsuccessful challenges to the CRTC's actions in the film distribution area, the USTR has indicated that it will continue to closely monitor the effect of these policies on U.S. interests, including possibly taking appropriate remedies under either GATT 1994 (WTO) or NAFTA.

In March 1997, Canadian distribution interests urged the CRTC to impose similar conditions respecting the licensing of video-on-demand. The U.S.-based studios opposed this further application of these restrictive conditions. The CRTC decision is expected imminently.



### *E. Telecommunications Policy*

In the recently concluded WTO negotiations on basic telecommunication services, Canada retained a 46.7% limit on foreign ownership, a requirement for "Canadian control" of basic telecom facilities, and a routing restriction to promote the use of Canadian facilities for domestic traffic. The routing restrictions are with regard to both domestic Canadian and international traffic, but the international traffic restrictions will be phased out over time. These restrictions have implications for cultural industries given the likelihood in this age of convergence of the telcos being permitted to be carriers of entertainment product in competition with the cable companies.

### *F. Possible Canadian Complaints Against the United States*

Canada has, until very recently, pursued its cultural policies only on the domestic front, whether through the CRTC, Investment Canada, the tax system, or the postal system. Unlike the USTR which carefully documents each year in its National Trade Estimates Canadian barriers to U.S. cultural industry exports and investment, the Canadian Department of Foreign Affairs and International Trade (DFAIT) in its annual "Register of U.S. Barriers to Trade" published at the beginning of April each year rarely mentions U.S. measures impacting adversely on the export of Canadian cultural products. In the April 1, 1997, sixteen-page *DFAIT Report on United States Barriers*, there is no mention of cultural industries other than a cryptic reference to section 301 of the Trade Act of 1994, and the situation where the USTR initiated a section 301 investigation against Canada based on the petition filed by Country Music Television (CMT). The DFAIT Report noted that USTR on February 6, 1996 had made a determination that certain Canadian broadcasting practices are discriminatory, but the same report also noted that the companies involved in the CMT dispute had signed an agreement thus ending the dispute, subject to ongoing U.S. monitoring.

One would have thought that the DFAIT Report might have referenced the unprecedented joint letter dated July 1, 1996 sent to the Chairman of the Federal Communications Commission (FCC) by the USTR, the U.S. Department of State, the U.S. Department of Justice, and the U.S. Department of Commerce. This letter was in the context of applications filed by two U.S. companies, TelQuest Ventures and Western Tele-Communications Inc., for satellite licenses making use of the facilities of Telesat Canada. The applications were subsequently denied by the FCC. The joint letter which opposed the grant of licenses under

these conditions raised questions of foreign trade, or competition policy within the jurisdiction of the U.S. executive branch and was based on the fact that the Government of Canada had not formally authorized Telesat to launch satellites into the Canadian orbital slots for the purposes described in the applications.

This unprecedented intervention to deny two U.S. cable companies access to a Canadian satellite facility under a negotiated arrangement made specific reference to both Canadian content restrictions and Canadian licensing restrictions. Respecting content, the joint letter noted:

Canada discriminates against U.S. and other foreign programmers and service providers in a number of ways. For example, Canada imposes extensive content restrictions on television and cable broadcasting including a requirement that the direct-to-home (DTH) service providers offers a preponderance (a minimum of 50%) of Canadian content. Further, these regulations are subject to unpredictable change after a nontransparent government review. As one result of this uncertainty, a U.S. DTH pay audio service was twice granted a broadcasting license only to have it overturned each time to allow consideration of whether more Canadian content should be required.

On the licensing restrictions in Canada, the joint letter stated:

The Government of Canada also maintains restrictions over the use of non-Canadian satellites for the distribution of telephone and broadcasting services to Canada. The Canadian government would not allow a U.S. satellite to provide DTH services to Canada—the exact analogy of the TelQuest and WTCI proposals. Even if the Government of Canada were to allow U.S. satellites to offer DTH service to Canada, Canada's content restrictions would prohibit a U.S. DTH provider (or its Canadian affiliate) from offering its DTH service to Canadian customers. The Government of Canada allows a temporary exception to these licensing restrictions if there is no available Canadian satellite, but that does not guarantee that the license will be available or renewable for a specific license term. The Government could revoke the authorization at any time that a Canadian satellite becomes available.

Thus, we see really for the first time, U.S. administrative and regulatory action brought to bear as a form of indirect retaliation for Canadian content and licensing restrictions, as outlined above. Why the DFAIT, in its *April 1, 1997 Report on U.S. Barriers*, did not reference this unprecedented joint intervention as a barrier to Canadian export of telecommunication services is a curious oversight, to say the least.

#### IV. THE CANADIAN VIEW OF THE U.S. PERSPECTIVE

Perhaps surprisingly, Canada has never really feared retaliatory measures of "equivalent commercial effect" under FTA/NAFTA because Canada, with one exception, has been quite careful in framing its cultur-

al initiatives that are not inconsistent but for the "cultural industries" exclusion. This certainly appears to be the case with respect to investment restrictions on film and television distribution and book publishing, and Canadian content and distribution requirements on television, DTH pay-per-view, and radio. Only with respect to magazines has Canada crossed the line. The tariff prohibition and preferential postal rates were found to violate "national treatment." But these measures were in place long before FTA or NAFTA. Even the impugned eighty percent excise tax imposed on advertising in split-run magazines was purported to be country-neutral and, therefore, not inconsistent with Canada's international trade obligations, although, as the WTO panel concluded, this was more in theory than in practical application.

The Canadian view of the U.S. perspective on respecting culture comes down to a simple explanation. "Cultural industries" is not a term that the United States understands or appreciates on a philosophical level, notwithstanding its precise definition in both the FTA and NAFTA. If there has to be a term, the Americans prefer "entertainment business."

The best explanation I have heard of the American psyche comes from U.S. academic George Quester writing on the International Politics of Television in 1990:

Many Americans are relatively unaware of the extent of the success of their entertainment business in selling television programs abroad. Why do Americans pay so little attention to the outside world? Because all the world is fascinated by the Manhattan skyline and San Francisco Bay, by blue jeans and screen entertainment. When all roads led to Rome, the Romans were less worldly than world-dominant. When Britannia ruled the waves, the British did not study the world as much as sail around it.

Particularly when it comes to pop culture, Americans believe the Canadian stuff is the same as the American, maybe slightly warmed over. Canadians believe otherwise. As Pevere and Dymond observed in *Mondo Canuck*:

Canadian was distinct. Indeed, because the country was otherwise largely dominated by various forms of American media, the contrast was all the more stark: in the noisy din of U.S. network programming, the Canadian stuff stuck out like a stunned moose in the middle of the Trans-Canada Highway.<sup>10</sup>

Americans believe entertainment is a business just like any other business -- subject to the rules of free trade and the application of na-

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<sup>10</sup> PEVERE & DYMOND, *supra* note 4.

tional treatment by all parties to the FTA/NAFTA. And, until recently, the United States believed there was only one way to deal with discriminatory trade practices in the entertainment business, and that is through section 301 of the Trade Act of 1974.

I am sure my fellow panelist, John Ragosta, will have a detailed and sophisticated analysis of this measure which is much talked about and feared in the international trade community. So I am not going to be so bold as to go too far along this road. However, I do want to give a Canadian impression.

Generally, Canadians regard Section 301 as unilateral and coercive. In Canada we have tried to learn and understand the distinctions between a "Super 301," a "Special 301," and a "Regular 301". A Super 301 tends to be more like a shot gun aimed at countries cited by the U.S. government as engaging in "broad and consistent patterns of unfair trade practices" and mandating unilateral retaliation following consultations within strict time limits. A Special 301 is more like a big stick backed up by a high-powered rifle, with which the USTR is directed to identify countries which deny adequate and effective protection of intellectual property rights. Canada felt the threat of this U.S. big stick in 1994 for the first time in relation to its current and proposed policies related to magazine publishing.

A Special 301 is distinguished from a Regular 301 in that its investigations must be concluded in final determinations rendered within six months of initiation, subject to a three-month extension where complex issues are involved or where there is progress in bilateral negotiations for a settlement or where the target country is taking action to remedy the source of U.S. concern. Compare this six-to-nine-month timeframe to the standard twelve-to-eighteen-month timeframe for Regular 301 proceedings which we call the little stick, backed up by a low-powered rifle. In cases where the USTR determines that action is warranted under a Special 301, retaliation normally is triggered within thirty days following conclusion of the investigation, and the USTR retains broad discretion to trigger a wide variety of retaliatory measures.

A Regular 301 or a little stick was what then USTR Mickey Kantor used in invoking the first formal challenge to discriminatory Canadian magazine practices on March 11, 1996. He appears to have used this simply to provide some kind of time discipline to his invocation of dispute settlement procedures of the WTO. In fact, the Regular 301 stick dovetailed nicely with WTO procedures in that it simply allows the USTR to make a determination as to whether the Canadian practices are actionable under Section 301 "by no later than 30 days after the conclusion of the WTO settlement proceedings or 18 months after the initia-

tion of the Section 301 investigation, whichever is earlier." It looks like the time discipline of this little stick may have had some effect since the WTO is likely to complete its hearing of the Canadian appeal by July or August this year, whereas the eighteen-month period following the initiation of the Regular 301 little-stick investigation does not come until September 11, 1997.

In this sense, the Regular 301 authority is not as unilateral or coercive as the Special or Super 301 authority since it appears to accommodate the WTO dispute settlement process including the WTO obligations or rules established under GATT 1994. It remains to be seen whether Canada complies with the WTO ruling once appeal rights and compliance periods are exhausted, or whether the United States must resort to triggering retaliatory measures.

Canada appears to be capable and willing to accommodate the Regular 301 proceedings, whether initiated by the USTR or on petition of aggrieved private U.S. parties. Not only does the Regular 301 proceed on a more reasonable timeframe, but it implicitly acknowledges the rules-based multinational approach inherent in the WTO process which on a reciprocal basis can be of immense benefit to Canada and other WTO members who have significant trading relations with the United States.

This is a trend is in the right direction, in my view. In his March 11, 1996 announcement, USTR Mickey Kantor indicated that the magazine dispute with Canada is the third such matter that the Clinton administration had taken to the WTO since the establishment of the USTR Enforcement Unit in January, 1996. On the Canadian side, there have been five GATT panels established at Canada's request since 1989 to rule on U.S. trade practices, dealing with fresh, chilled, and frozen pork; alcoholic and malt beverages; softwood lumber; magnesium; and limits on the use of foreign tobacco. The Helms-Burton legislation related to Cuba is another U.S. measure which, until late March, 1997, appeared headed for the WTO at the behest of the Europeans, but with strong support from Canada. The deal worked out between the E.U. and the United States last week included U.S. commitments to amend or suspend parts of Helms-Burton in return for E.U. commitments to develop rules covering dealing with expropriated property within the framework of the OECD's Multilateral Agreement on Investment (MAI).

Whether you want to call it "cultural industries" or the "entertainment business," serious trade disputes between Canada and the United States which are incapable of resolution through bilateral consultations are more likely to be resolved in Geneva or Paris than in Washington or Ottawa. For Canada, this is not a bad result in the bigger scheme of

things.

## V. CONCLUSION

At the outset of this Article, I noted that a more appropriate title for this discussion might have been "Canada-U.S. Cultural Industries Disputes Outside of NAFTA." In making this observation, I did not mean to suggest that the cultural industries exemption in the context of the FTA/NAFTA is not a significant development in Canada-U.S. trade relations simply because it has never been, and may never be, invoked. Quite to the contrary, the very existence of the cultural industries exemption, irrespective of its lack of use, is hugely significant in terms of what it *does not* accomplish. The fact that neither the United States or Canada has ever sought formal recourse to the provision—either to justify a discriminatory action or to explain a retaliatory measure—suggests to many that this "tit-for-tat" approach to conflict resolution has only frozen the parties in their respective ideological spheres, each side feeling that it gained the upper hand in the trade negotiation if only on paper. But one wonders how long such posturing can continue.

As the examples of potential cultural trade disputes continue to mount, the strategy of avoidance is increasingly giving way to renewed consideration of how best to achieve cultural goals while keeping markets open. Ultimately, the disquieting experience with the enigmatic cultural industries exemption may be an incentive to create realistic and workable trade rules, as opposed to trade exemptions, that go much further in striking this balance.

The WTO panel decision on magazines may represent somewhat of a watershed for the cultural industries exemption in Canada. By resorting to excessive measures in the form of the eighty-percent tax on advertising in split-run magazines, the Canadian government effectively exposed its cultural industries to the national treatment requirements of GATT 1994 by precipitating the successful U.S. challenge at the WTO. Barring an unexpected turn about at the WTO appellate body, Canada will have to bring its laws into conformity with GATT 1994 as defined by the WTO panel, revoke the prohibitive tariff and preferential postal rates, and repeal the eighty-percent excise tax. This will lead to domestic pressure to come up with other measures or subsidies to satisfy the political demand for uniquely Canadian magazines.

As a result, the ground has shifted away from the rather crude "tit-for-tat" mechanism established by FTA/NAFTA based on an "exemption-retaliation for inconsistency" and moved over to the rules-based approach of the WTO in interpreting GATT 1994, the GATS, and the

MAI. Granted, both the GATS and MAI have a cultural industries carve out of a sort. But, significantly, the WTO panel on magazines found that GATT 1994 and GATS can coexist without either taking priority over the other, and that there are several precedents which permit a consideration of trade and services, including advertising services, under GATT 1994.

The practical short-run effect for Canada after eighteen months will be that there will be fewer protections for its magazine industry than it had before it introduced the eighty-percent excise tax. For the United States, the retaliation was far more effective under the WTO since there was no "equivalent commercial effect" limitation. Moreover, the WTO panel decision will have far more authoritative impact in Europe and Asia, where U.S. entertainment interests are regularly subject to local discriminatory practices than would a NAFTA panel decision upholding U.S. retaliatory measures against Canada "of equivalent commercial effect."

In Canada, the setback on magazines has a bright side to it. A public policy debate has been precipitated on how best to support and develop Canadian culture. Shortly after news of the WTO panel was released in January, International Trade Minister Art Eggleton delivered a milestone speech at Osgoode Hall Law School of York University entitled "Can Canada Maintain its Cultural Identity in the Face of Globalization?" He questioned whether Canada's cultural protections which limit foreign investment in cultural industries and Canadian content rules are actually hindering Canada's exports of cultural goods and services. The Trade Minister indicated that he thinks the current method of dealing with culture in international trade agreements through exemptions (as was done in the NAFTA) is no real protection at all for Canada's cultural interests. A better approach, according to Mr. Eggleton, might be to formulate concrete rules for trade in cultural products.

Just two weeks later, Canadian Heritage Minister Sheila Copps countered with some musings of her own, suggesting that the CRTC impose an "expenditure cap" on the purchase of non-Canadian television programming to leave more money free for Canadian programming, or revisions to Canadian content rules by excluding sports and news, or requiring radio broadcasters to cluster their Canadian content in prime time.

These public musings of Ministers have precipitated further policy discussion as to Canada's approach to culture which, in my view, is a healthy sign that Canada is recognizing global changes and the need for adjustment to a rules-based international environment where culture is enhanced based on its on intrinsic merit without resorting to trade dis-

torting measures. A rules-based approach without reference to economic power should benefit a medium-sized market economy such as Canada's. One policy idea that has been advanced in a paper prepared by Daniel Schwanen of the C.D. Howe Institute and released on April 22nd is the de-linking of foreign-ownership from the delivery of Canadian cultural products, suggesting that there is no automatic connection between the cultural content embodied in the product and the ownership of the enterprise delivering or marketing the product. The truth in this premise is demonstrated by Seagram's acquisition of control of Universal studios in which case Canadian ownership has had no apparent impact on the output of Canadian culture by that studio. While the relaxation of foreign investment restrictions is heresy to some in Ottawa, it does offer an interesting solution to the Canadian conundrum. Mr. Schwanen notes that the policy implications of this approach for foreign investment are fairly clear:

Subsidies towards products aimed at a Canadian audience and the awarding of "shelf space" for such products should be open to foreign owners who can make an original contribution to the Canadian market . . . [and] in the vast majority of cases this will involve making use of Canadian talent and carrying Canadian perspectives.

The WTO magazine decision has clearly precipitated this debate. The events of the next twelve to eighteen months following the election should result in a more modern and global approach towards developing Canadian culture than has prevailed over the past twenty years with its more protectionist approach. Significantly, I believe that it will be Canadian artists seeking to access international markets and distribution, bolstered by political support from Canadian owners of cultural enterprises pursuing their own self interest, who will eventually carry the day in this debate in Canada. The regime that will result, while not totally to the liking of the U.S. entertainment establishment, will have a clear and more fairly balanced set of rules that allow for foreign participation on a level Canadian playing field.

And let us not forget that what is sauce for the goose is sauce for the gander. Just as the USTR found it effective and convenient to take Canada to the WTO on magazines, so can Canada and the Europeans take the United States to the WTO on matters such as Helms-Burton or licensing and foreign ownership of telecommunications services.

In summary, the bilateral relationship between Canada and the United States respecting cultural industries and the entertainment business is tending to be subsumed over time by the multilateral framework provided by the WTO or the OECD for both negotiations and dispute settle-



ment. And in a global economy, is this not in everyone's interest?